

UNITED STATES DISTRICT COURT  
EASTERN DISTRICT OF WASHINGTON

RICHARD CONRAD,  
Plaintiff,

V.

ACE PROPERTY & CASUALTY INSURANCE  
COMPANY and RAIN & HAIL, LLC,

## Defendants.

No. CV-05-5117-FVS

ORDER DENYING PLAINTIFF'S  
MOTION FOR SUMMARY JUDGMENT  
AND GRANTING DEFENDANTS'  
CROSS-MOTION FOR SUMMARY  
JUDGMENT

**BEFORE THE COURT** are cross motions for summary judgment. The Court heard oral argument on these motions on June 2, 2006. Plaintiff was represented by Nicholas Gellert. Defendants were represented by Sean Bourtz.

## I. BACKGROUND<sup>1</sup>

Plaintiff Richard Conrad owns and operates a fruit orchard in Franklin County, Washington. Plaintiff purchased from Defendant Ace Property and Casualty Insurance Company ("Ace") an Adjusted Gross Revenue Pilot Insurance Policy ("Policy"). Defendant Rain & Hail, LLC ("Rain and Hail"), acted as Ace's agent in administration of the Policy. The Policy was issued pursuant to a Federal Crop Insurance Corporation ("FCIC") pilot program, under the auspices of 7 U.S.C. §

<sup>1</sup> The parties agree there are no disputed issues of material fact and that this case is appropriate for resolution on summary judgment.

1 1501 et seq. The FCIC did not issue Plaintiff's Policy; rather the  
2 Policy was reinsured by FCIC. In this regard, the Policy states:

3 This insurance policy is reinsured by Federal Crop  
4 Insurance Corporation (FCIC) under the provisions of the  
Federal Crop Insurance Act (7 U.S.C. 1501 et seq.) (Act).  
5 All provisions of the policy and rights and  
responsibilities of the parties are specifically subject to  
the Act. The provisions of the policy may not be waived or  
varied in any way by the crop insurance agent or any other  
agent or employee of FCIC or the company. In the event we  
7 cannot pay your loss, your claim will be settled in  
accordance with the provisions of this policy and paid by  
8 FCIC. No state guarantee fund will be liable for your  
loss.

9 Policy, at 1. The Policy contains the following definition of  
10 "Policy":

11 The agreement between you and us consisting of the accepted  
application, these provisions, Special Provisions,  
actuarial documents, and the applicable regulations  
published in 7 C.F.R. chapter IV.

14 Policy, at 3.

15 The key to coverage under this Policy is what is referred to as  
16 the Approved Adjusted Gross Revenue ("Approved AGR"). From the  
17 Approved AGR, the amount of coverage, and, in turn, the annual  
18 premiums are determined. See Policy, Section 6. The Approved AGR is  
19 also the base from which the amount of indemnity owed to the insured  
20 is determined in the event of a loss. See Policy, Section 11.

21 Plaintiff suffered a loss against his expected orchard revenue  
22 for the 2004 crop year due to harsh weather conditions and submitted  
23 a claim for \$1,021,598. Plaintiff's claim was calculated by using an  
24 Approved AGR of \$2,341,360. Conversely, Defendants calculated  
25 Plaintiff's 2004 crop loss at \$516,686, using an Approved AGR of  
26 \$1,640,092. Plaintiff seeks additional indemnity in the amount of

1 \$486,008 and prejudgment interest. This figure is the difference  
2 between Plaintiff's calculated loss of \$1,021,598, and Defendants'  
3 calculated loss of \$516,686, less the additional premium payment of  
4 \$18,904 that Plaintiff would be required to pay if additional  
5 coverage is extended. Defendants request the Court enter judgment in  
6 their favor, concluding that the indemnity payment to Plaintiff in  
7 the amount of \$516,686 satisfied Defendants' obligations under the  
8 terms of the Policy.

## 9 **II. DISCUSSION**

### 10 **A. Jurisdiction**

11 Plaintiff filed this action for damages in Franklin County  
12 superior court. Defendants timely removed the action to federal  
13 court. 28 U.S.C. § 1441. The Court has original jurisdiction over  
14 this action based on diversity of citizenship pursuant to 28 U.S.C. §  
15 1332(a) because Ace is a Pennsylvania corporation, Rain and Hail is  
16 an Iowa corporation, and Plaintiff is a citizen of Washington state.  
17 Since federal jurisdiction in this case is based on diversity of  
18 citizenship, the Court must apply the substantive law of the state of  
19 Washington. *Erickson v. Desert Palace, Inc.*, 942 F.2d 694, 695 (9th  
20 Cir 1991) (citing *Erie R.R. v. Tompkins*, 304 U.S. 64, 58 S.Ct. 817,  
21 82 L.Ed. 1188 (1938)).

### 22 **B. Rules of Construction for Contract Interpretation**

23 Interpretation of an insurance contract is a question of law.  
24 *Quandrant Corp. v. American States Ins. Co.*, 154 Wash.2d 164, 171,  
25 110 P.3d 733, 737 (2005). Insurance contracts are construed as  
26 contracts. *Id.* An insurance contract should be considered as a

1 "whole" and given a "fair, reasonable, and sensible construction as  
 2 would be given to the contract by the average person purchasing  
 3 insurance." *Id.* (citation and internal quotation marks omitted). If  
 4 the policy language is clear and unambiguous, [the Court] must  
 5 enforce it as written; [the Court] may not modify it or create  
 6 ambiguity where none exists." *Id.* A clause is ambiguous only "when  
 7 on its face, it is fairly susceptible to two different  
 8 interpretations, both of which are reasonable." *Id.* If a clause is  
 9 ambiguous, the Court may rely on extrinsic evidence of the intent of  
 10 the parties to resolve the ambiguity. *Id.* "Any ambiguity remaining  
 11 after examination of the applicable extrinsic evidence is resolved  
 12 against the insurer and in favor of the insured." *Id.* The  
 13 "expectations of the insured may not override the plain language of  
 14 the contract." *Id.*

### 15       C.     **The Policy**

16       The Policy defines "Approved AGR" as:

17       The simple average of the AGR income history you included  
 18       on your farm report, adjusted to reflect any expected  
 19       increase or reduction in allowable income for the insurance  
 20       year (see section 5).

21       Policy at 2. The referenced Section 5 of the Policy contains  
 22       multiple subparts, but subpart (e) is the only relevant subpart  
 23       dealing with adjusting the AGR to reflect increases and decreases in  
 24       an insured's income. It states, in relevant part:

- 25           (e) Your average AGR income history will be adjusted to  
 26           reflect any reduction in potential revenue for the  
 27           insurance year caused by changing the agricultural  
 28           commodities produced from your farming operation, the  
 29           size of your farming operation, your share, market  
 30           conditions or damage to any crop occurring prior to the

beginning of the insurance period, or any other factor that could result in less allowable income for the insurance year than the simple average of your AGR income history.

- (1) We will make this reduction based on the information contained in your farm report, our inspection of any damaged crop, and our estimate of the effect of these changes or conditions.
- (2) ...
- (3) If you can prove that your allowable income for the insurance year will be higher than the average of your AGR income history, we **may** establish your approved AGR at a greater amount than the average.
- (4) If we establish your approved AGR at a greater amount than the average of your AGR income history, the indexed average expenses will be calculated as follows:

Policy at 6 (emphasis added).

The above quoted provisions in the Policy contain detailed descriptions of how expenses will be calculated if the approved AGR is higher or lower than the five year average. However, it is silent with respect to how the income side of the equation is set to arrive at an approved AGR that is higher or lower than the five-year average. With respect to a reduced income, the Policy says that Defendants may make an "estimate". See Policy, Section 5(e)(1). With respect to increased income from expanding operations, the Policy simply says that Defendants "may" set the Approved AGR above the five-year average when expected income is higher than the average. See Policy, Section 5(e)(3).

Here, Plaintiff's five-year average income history from 1998 through 2002 was \$1,620,644. However, Plaintiff claims his expected income for the 2004 crop year was going to be much higher than this average because in the last few years he had replaced damaged and

1 out-of-date trees. Thus, Plaintiff contends his Approved AGR must be  
2 adjusted upward from the average of his five-year income history to  
3 his expected income for 2004, or \$2,341,360. Plaintiff argues the  
4 Policy requires that the Approved AGR be established to reflect any  
5 increases or decreases from the five year average because the Policy  
6 defines Approved AGR as the "average of the AGR income history ...  
7 adjusted to reflect any expected increase[.]" Policy, at 2 (emphasis  
8 added). Plaintiff acknowledges that Section 5(e) of the Policy  
9 indicates only that the Approved AGR "may" be set higher than the  
10 average. However, Plaintiff contends "may" must be interpreted to  
11 mean "shall" or the promise to adjust in the definition of "Policy"  
12 would become illusory. Finally, Plaintiff contends that the Policy  
13 is ambiguous with respect to how the Approved AGR is to be set in  
14 circumstances of increased expected income. Thus, Plaintiff argues  
15 the Policy has to be given the interpretation that favors the  
16 broadest coverage.

17 On the other hand, Defendants contend Plaintiff's Approved AGR  
18 must be calculated pursuant to the procedures set forth in the  
19 Adjusted Gross Revenue Standards Handbook ("Handbook") published by  
20 the FCIC. Defendants contend the Policy is not ambiguous with  
21 respect to how the Approved AGR should be calculated in circumstances  
22 of increased expected income because the terms in the Policy  
23 establish the use of the Handbook's indexed average.

24 **D. The Handbook**

25 Defendants contend the Handbook's definition of Approved AGR and  
26 the indexing procedure set forth in the Handbook has been

1 incorporated by reference into the Policy. First, Defendants note  
2 that the Policy only states that Defendants *may* determine Plaintiff's  
3 Approved AGR should be set higher than his previous five-year  
4 average. Second, Defendants point to the section of the Policy that  
5 states: "All provisions of the policy and rights and  
6 responsibilities of the parties are specifically subject to the Act.  
7 The provisions of the contract may not be waived or varied in any way  
8 by the crop insurance agent or any other agent or employee of FCIC or  
9 the company." Third, Defendants point to a section in the Policy  
10 dealing with the insurer's duties in the event of damage or loss.  
11 This section states, in relevant part,

12 We recognize and apply the claim adjustment and other  
13 procedures established or approved by FCIC.

14 Policy, at 8. For these reasons, Defendants argue the Policy  
15 requires use of the FCIC procedures, which are set forth in the  
16 Handbook.

17 The Handbook defines Approved AGR as:

18 The simple average of the AGR income history included on  
19 the insured's Farm Report adjusted to reflect any expected  
20 increase (Indexed income) or reduction (total expected  
21 income) or reduction in allowable income for the insurance  
22 year [See Part 2, Section 19, Par. B].

23 The referenced "Part 2" of the Handbook is entitled  
24 "Underwriting", see Handbook, at 26, and the referenced Section 19 is  
25 entitled "Calculation of AGR". See Handbook, at 44. Using the  
26 indexing procedures in Section 19 of the Handbook, Defendants  
calculated Plaintiff's 2004 Approved AGR at \$1,640,092. This was an

<sup>1</sup> upward adjustment of \$19,448 from Plaintiff's five-year average.<sup>2</sup>

The Court agrees with Plaintiff in that the term "may" in Section 5(e) of the Policy can only mean "shall" or the contract becomes illusory. Here Plaintiff proved that his expected income for the 2004 crop year was going to be higher than the average of his AGR income history. Consistent with the directive in Section 5(e), Defendants established Plaintiff's Approved AGR at a greater amount than the average: \$19,448 higher than his average. However, Plaintiff disputes Defendants use of the Handbook and wants to use his full expected income for his Approved AGR. To accept Plaintiff's contention, the Court would need to conclude that the Policy is ambiguous with respect to how the Approved AGR is to be set in circumstances of increased expected income.

14 However, the Court cannot conclude the language in the Policy is  
15 ambiguous. Although Section 10 of the Policy does not specifically  
16 identify which claim adjustment procedures may be applied, Section 10  
17 does state that the insurer will recognize and apply those claim  
18 adjustment procedures "established or approved by FCIC." Here,  
19 Plaintiff does not dispute that the Handbook was established and  
20 approved by the FCIC. Although Plaintiff argues Section 10 is only  
21 applicable to loss claims, and not the determination of an insured's  
22 Approved AGR, Plaintiff acknowledges that the Approved AGR is crucial  
23 in determining each and every loss claim. Thus, when the Court reads

2 Plaintiff's revenue from his orchard for the years 1998  
25 through 2002 ranged from \$1,474,377 to \$1,836,600 for a five-year  
26 average of \$1,620,644.

1 the Policy as a "whole", Section 10 is certainly applicable to  
2 determining the Approved AGR when calculating a claim for loss or  
3 damage. Although the Policy may not provide for the result Plaintiff  
4 expected, the "expectations of the insured may not override the plain  
5 language of the [Policy]." *Quandrant Corp.*, 154 Wash.2d at 171, 110  
6 P.3d at 737. The Court concludes Defendants' use of the Handbook is  
7 provided for by the terms of the Policy. Therefore, the Court  
8 determines Defendants' indemnity payment to Plaintiff in the amount  
9 of \$516,686 satisfied Defendants' obligations under the terms of the  
10 Policy. Accordingly,

11           **IT IS HEREBY ORDERED** that Plaintiff's Motion for Summary  
12 Judgment (**Ct. Rec. 10**) is **DENIED** and Defendants' Cross-Motion for  
13 Summary Judgment (**Ct. Rec. 16**) is **GRANTED**.

14           **IT IS SO ORDERED.** The District Court Executive is hereby  
15 directed to enter this Order, furnish copies to counsel, **ENTER**  
16 **JUDGMENT FOR DEFENDANTS** and **CLOSE THE FILE**.

17 || **DATED** this 5th day of June, 2006.

18 \_\_\_\_\_ *s/ Fred Van Sickle*  
19 Fred Van Sickle  
United States District Judge